



STATE BOARD OF EQUALIZATION STAFF LEGISLATIVE BILL ANALYSIS

Date Introduced: **2/20/04**

Bill No: **AB 2802**

Tax: **Sales and Use Tax**

Author: **Horton**

Board Position:

Related Bills:

BILL SUMMARY

This bill would require the Board to grant to a qualified person, as defined, a sales and use tax offset, in an amount equal to 1 percent of a qualified person's state sales and use tax liability during a specified 12 month period.

ANALYSIS

Current Law

Existing law imposes a sales tax on retailers for the privilege of selling tangible personal property at retail. In general, every person, firm, partnership, corporation, etc., engaging in the business of selling tangible personal property that is subject to the tax when sold at retail is required to apply to the Board for a seller's permit.

Under the law, holders of seller's permits are required to file returns with the Board reporting their gross receipts and the amount of tax due. Depending on the amount of tax that is estimated to be due, return periods will generally consist of either calendar quarters, calendar months, calendar years, or fiscal years. Current law provides that the taxes and return are due to the Board on or before the last day of the month following each reporting period.

Current law provides that any person who fails to pay any tax to the state within the required time period shall pay a penalty of 10 percent of the tax due, in addition to the amount of the tax due, plus interest. Additionally, any person who fails to file a return within the required time period shall pay a penalty of 10 percent of the amount of taxes due. These penalties are limited to a maximum of 10 percent, so if a person fails to remit the taxes due and also fails to file the required return, the taxpayer is assessed only one 10 percent penalty.

Proposed Law

This bill would add Section 6458 to the Revenue and Taxation Code to provide that the Board shall grant to a qualified person a sales and use tax offset, to be claimed by that person against that person's state sales and use tax liability (5.25 percent rate). This bill defines a qualified person as a person who operates a new trade or business in this state and files all necessary returns with the proper remittance in a timely manner. The sales and use tax offset provided in this bill would be an amount equal to 1 percent of the state sales and use tax liability (5.25 percent rate) incurred during the first 12 months of business operations, but not to exceed \$525.

This staff analysis is provided to address various administrative, cost, revenue and policy issues; it is not to be construed to reflect or suggest the Board's formal position.

Background

Of the 46 states and the District of Columbia that impose a sales and use tax, 28 of these provide taxpayers with a credit or discount. Currently, California is one of 18 states that does not provide any reimbursement to compensate taxpayers for collecting and remitting sales and use taxes in a timely manner.

Assembly Bill 1936 (Horton), introduced during the 2002 Legislative Session, contained similar provisions as this bill. These provisions were removed from the bill when the bill was amended on May 23, 2002.

COMMENTS

1. **Sponsor and purpose.** This bill is sponsored by Board Member Claude Parrish. The purpose of this bill is to encourage compliance by providing an economic incentive for a new trade or business in this state to timely file the sales and use tax return and remit the proper amount of tax due.
2. **Offset allowed against state rate only.** The proposed offset would be calculated based on 1 percent of the state tax rate. The state tax rate is currently 5 percent. Laws scheduled to become operative July 1, 2004 would have raised the state rate to 5.5 percent. The cap of \$550 in the bill was based on \$10,000 in taxable measure and the assumption that the state rate would be 5.5 percent. However, due to the recent passage of Proposition 57, the state rate is now scheduled to increase to 5.25 percent as of July 1, 2004. Proposed amendments would adjust the cap to \$525.
3. **Proposed amendments.** As currently written, this bill would grant an offset only after the taxpayer has filed all returns due during a twelve-month period. Proposed amendments would allow the taxpayer to claim the offset on any and all returns filed covering the first twelve months of business operations, up to the maximum amount of \$525 per taxpayer. This would allow some taxpayers to realize the benefits of the proposed offset much quicker.
4. **Benefits for the state.** Providing an offset for new taxpayers can have many benefits for the state. The financial incentive would partially offset the cost for new taxpayers to file their tax returns, creating a sense of goodwill between the Board and taxpayers. For certain types of sales a vendor discount may provide a sufficient incentive to improve taxpayer compliance, resulting in additional reporting of taxable sales. One state we contacted, the South Carolina Department of Revenue, mentioned that they believe their vendor discount program encourages the timely filing and payment of the sales tax and it also promotes voluntary compliance. Unfortunately, South Carolina staff told us that they did not have statistical data to support this conclusion.

COST ESTIMATE

A detailed cost estimate is pending.

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REVENUE ESTIMATE

This bill would provide new permittees a sales and use tax offset (or vendor discount) of one percent of sales and use tax payments made, with a maximum discount payment of \$525 per taxpayer. The bill only applies to the state portion of the sales tax, that as of July 1, 2004, is a rate of 5.25 percent.¹

Background, Methodology, and Assumptions

The Sales and Use Tax Department (SUTD) reports that 117,640 new permits were issued in 2000, including those that later closed out before the end of the year (see table on next page). The table also shows average sales and use tax revenues, categorized by five time period reporting bases of taxpayers with full-time and part-time businesses. The average statewide sales and use tax rate is 7.92 percent. We assume that the reported tax by these new permittees also averages 7.92 percent. The proposed vendor discount is only applied to the state portion (5.25 percent) of the average state and local tax rate of 7.92 percent, which requires the middle column in the table that multiplies the originally reported tax revenue by the factor (5.25 / 7.92). As shown in the table, we estimate that the bill will cost the state approximately \$6.4 million per year.

According to our estimate of the distribution of new taxpayer numbers, the vendor discounts to most taxpayers would be very small. On average, 62 percent of the new taxpayers would receive discounts of less than \$10 per year. At the opposite extreme, 8 percent of new taxpayers would receive the maximum discount of \$525 per year.

For certain types of sales a vendor discount may provide a sufficient incentive to improve taxpayer compliance, resulting in additional reporting of taxable sales. However, the revenues from compliance improvement are impossible to accurately estimate. Two unknown figures would need to be estimated: (1) noncompliance revenues from current taxpayer practices that potentially could become reported under the proposal, and (2) the percentages of such noncompliance revenues that taxpayers would be likely to pay under the bill.

¹ This revenue estimate was prepared under the assumption that the bill will be amended to: (1) eliminate the 12-month waiting period that is currently in the bill and, (2) change the maximum amount from \$550 to \$525 per taxpayer.

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**Proposed Sales and Use Taxpayer Discount for New Accounts
No Waiting Period, Maximum Discount of \$525 Per Taxpayer**

**Type of Return and Reporting
Basis**

	Total New	Average	Ave. Reported	Annual	Total
	Accounts	Reported	Times	Discount	Annual
		Tax Due	(5.25/7.92)	1% or \$525	Discount
		(Dollars)	(State Rate	(Dollars)	(Dollars)
			Portion)		

Reporting Basis:**Full Time**

Monthly	8,653	\$9,646.07	\$6,394.18	\$63.94	\$553,288
Quarterly	26,095	\$3,300.05	\$2,187.53	\$21.88	\$570,837
Quarterly (Prepayment)	9,600	\$107,824.52	\$71,474.59	\$525.00	\$5,040,000
Fiscal Yearly	16,838	\$588.55	\$390.14	\$3.90	\$65,691
Yearly	26,968	\$371.04	\$245.95	\$2.46	\$66,329
Subtotal Full Time	88,154	n/a	n/a	n/a	\$6,296,145

Reporting Basis:**Part Time**

Monthly	351	\$2,689.19	\$1,782.61	\$17.83	\$6,257
Quarterly	3,387	\$1,042.58	\$691.10	\$6.91	\$23,408
Quarterly (Prepayment)	115	\$36,594.59	\$24,257.78	\$242.58	\$27,896
Fiscal Yearly	11,207	\$112.42	\$74.52	\$0.75	\$8,352
Yearly	14,426	\$106.44	\$70.56	\$0.71	\$10,179
Subtotal Part Time	29,486	n/a	n/a	n/a	\$76,091

Totals	117,640				\$6,372,236
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Revenue Summary

The total ongoing annual revenue loss of this bill would be approximately \$6.4 million. Since the proposed law would take effect January 1, 2005, the revenue impact would be about half of this amount, or \$3.2 million in fiscal year 2004-05.

Analysis prepared by:	Bradley E. Miller	916-445-6662	03/10/04
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Revenue estimate by:	Joe Fitz	916-323-3802
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Contact:	Margaret S. Shedd	916-322-2376
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